

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions	:	
of	:	
4 U CONVENIENCE, INC.	:	DETERMINATION
AND AHMED ESSANI	:	DTA NOS. 824971 AND 824972
	:	
for Revision of Determinations or for Refund of	:	
Sales and Use Taxes under Articles 28 and 29 of the	:	
Tax Law for the Period December 1, 2006 through	:	
August 31, 2009.	:	

Petitioners, 4 U Convenience, Inc., and Ahmed Essani, filed petitions for revision of determinations or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 2006 through August 31, 2009.

A hearing was held before Thomas C. Sacca, Administrative Law Judge, in New York, New York, on September 5, 2013, at 10:30 A.M., with all briefs to be submitted by February 6, 2014, which date commenced the six-month period for issuance of this determination. Petitioner Ahmed Essani appeared pro se and as president of 4 U Convenience, Inc. The Division of Taxation appeared by Amanda Hiller, Esq. (Michael B. Infantino, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly disallowed a portion of the prepaid sales tax credits claimed by 4 U Convenience, Inc., for the period December 1, 2006 through August 31, 2009.

FINDINGS OF FACT

1. Petitioner, 4 U Convenience, Inc., operated a convenience store selling taxable and non-taxable items, including cigarettes. Petitioner, Ahmed Essani, was the president of the corporation.

2. An audit appointment letter, dated October 19, 2009, was mailed by the Division of Taxation (Division) to the corporation to review the corporation's sales and use tax records for the period December 1, 2006 through August 31, 2009. The appointment was scheduled for November 11, 2009 and requested that specific records pertinent to the audit period be made available at that time, including: sales tax returns; federal income tax returns; New York State corporation tax returns; the general ledger; general journal and closing entries; all exemption documentation to support nontaxable sales; chart of accounts; fixed asset purchase and sales invoices for the audit period; expense purchases; merchandise purchases; bank statements, canceled checks and deposit slips for all bank accounts maintained by the corporation; cash receipts journal; cash disbursement journal; the corporate book; depreciation schedules for the audit period; State Liquor Authority license in effect for the audit period; utility bills; guest checks; and cash register tapes for the audit period.

3. The corporation failed to provide to the auditor detailed cash register tapes, a day book, bank statements, federal income tax returns and any record of check disbursements. Although some invoices of cigarette purchases were provided, they were insufficient to substantiate the prepaid sales tax credits claimed. As a result, the auditor concluded that the records maintained were inadequate to accurately determine the corporation's sales and tax liability for the audit period.

4. In order to verify the amount of prepaid sales tax claimed by the corporation on its purchases of cigarettes, the auditor wrote the corporation's suppliers to obtain the amounts of cigarettes sold to the corporation. Using the corporation's cigarette purchase invoices and the information obtained from the third-party suppliers, the auditor determined total audited cigarette purchases (cartons). Total cartons purchased was multiplied by the appropriate tax rate to arrive at audited prepaid sales tax on cigarette purchases. This amount was subtracted from the prepaid sales tax claimed on the corporation's tax returns for the audit period to determine the amount of disallowed prepaid sales tax claimed. The corporation had claimed \$30,963.00 in prepaid sales tax credits for the audit period, but at the time of the audit, only \$21,689.62 could be substantiated as having been actually paid to the third-party vendors. As a result, \$9,273.38 was initially disallowed and determined to be due.

5. In preparation for the hearing, the Division's witness noticed some mathematical errors in the workpapers and made adjustments and corrections that resulted in lowering the tax due. The witness's computations were done in detail and resulted in a greater allowance of prepaid sales tax paid to Coremark Midcontinent, Inc., one of the corporation's cigarette suppliers. Originally, the amount paid to Coremark was computed to be \$15,494.32. However, after reviewing the original workpapers, it was determined that prepaid sales tax to Coremark should be increased to \$16,148.22, resulting in a decrease to \$8,619.48 of the amount of sales tax due. Statutory penalty was imposed due to the corporation's inadequate records and underreporting and underpayment of tax due.

6. Petitioners did not produce any source documentation, such as cigarette purchase invoices, that would establish or support the amount of prepaid sales tax on cigarette purchases claimed on the corporation's sales tax returns.

7. On February 15, 2011, as a result of the field audit performed, the Division issued to petitioner 4 U Convenience, Inc., a Notice of Determination (assessment number L-035416436), asserting additional sales tax due of \$25,573.45, plus penalty and interest, for the period December 1, 2006 through August 31, 2009. On February 16, 2011, the Division issued to petitioner Ahmed Essani, as a responsible officer of 4 U Convenience, Inc., a Notice of Determination (assessment number L-035420249), asserting additional sales tax due of \$25,573.45, plus penalty and interest, for the period December 1, 2006 through August 31, 2009.

At the hearing, the Division conceded that the amounts assessed in the notices of determination are each to be reduced to \$8,619.48.

CONCLUSIONS OF LAW

A. Tax Law § 1105(a) imposes a sales tax on the receipts from every “retail sale” of tangible personal property except as otherwise provided in Article 28 of the Tax Law. A “retail sale” is “a sale of tangible personal property to any person for any purpose, other than . . . for resale as such . . .” (Tax Law § 1101[b][4][i]). Tax Law § 1135(a)(1) provides that “[e]very person required to collect tax shall keep records of every sale . . . and of all amounts paid, charged or due thereon and of the tax payable thereon, in such form as the commissioner of taxation and finance may by regulation require.” Every person selling or possessing large quantities of cigarettes is required to keep records for such periods. Such records shall show the number of cigarettes purchased, the price paid therefor, the person from whom such cigarettes were purchased and the amount of tax paid pursuant to Tax Law § 1103 (Tax Law § 1135[e]). Tax Law § 1103 requires the prepayment of sales tax on cigarettes.

B. Tax Law § 1138(a)(1) provides, in relevant part, that if a sales tax return was not filed, “or if a return when filed was incorrect or insufficient, the amount of tax due shall be determined

[by the Division of Taxation] from such information as may be available. If necessary, the tax may be estimated on the basis of external indices. . . .” (Tax Law § 1138[a][1].) When acting pursuant to section 1138(a)(1), the Division is required to select a method reasonably calculated to reflect the tax due. The burden then rests upon the taxpayer to demonstrate that the method of audit or the amount of the assessment was erroneous (*see Matter of Your Own Choice, Inc.*, Tax Appeals Tribunal, February 20, 2003).

C. The standard for reviewing a sales tax audit where external indices were employed was set forth in *Matter of Your Own Choice, Inc.*, as follows:

To determine the adequacy of a taxpayer’s records, the Division must first request (*Matter of Christ Cella, Inc. v. State Tax Commn.*, [102 AD2d 352, 477 NYS2d 858] *supra*) and thoroughly examine (*Matter of King Crab Rest. v. Chu*, 134 AD2d 51, 522 NYS2d 978) the taxpayer’s books and records for the entire period of the proposed assessment (*Matter of Adamides v. Chu*, 134 AD2d 776, 521 NYS2d 826, *lv denied* 71 NY2d 806, 530 NYS2d 109). The purpose of the examination is to determine, through verification drawn independently from within these records (*Matter of Giordano v. State Tax Commn.*, 145 AD2d 726, 535 NYS2d 255; *Matter of Urban Liqs. v. State Tax Commn.*, 90 AD2d 576, 456 NYS2d 138; *Matter of Meyer v. State Tax Commn.*, 61 AD2d 223, 402 NYS2d 74, *lv denied* 44 NY2d 645, 406 NYS2d 1025; *see also, Matter of Hennekens v. State Tax Commn.*, 114 AD2d 599, 494 NYS2d 208), that they are, in fact, so insufficient that it is “virtually impossible [for the Division of Taxation] to verify taxable sales receipts and conduct a complete audit” (*Matter of Chartair, Inc. v. State Tax Commn.*, 65 AD2d 44, 411 NYS2d 41, 43; *Matter of Christ Cella, Inc. v. State Tax Commn.*, *supra*), “from which the exact amount of tax due can be determined” (*Matter of Mohawk Airlines v. Tully*, 75 AD2d 249, 429 NYS2d 759, 760).

Where the Division follows this procedure, thereby demonstrating that the records are incomplete or inaccurate, the Division may resort to external indices to estimate tax (*Matter of Urban Liqs. v. State Tax Commn.*, *supra*). The estimate methodology utilized must be reasonably calculated to reflect taxes due (*Matter of W.T. Grant Co. v. Joseph*, 2 NY2d 196, 159 NYS2d 150, *cert denied* 355 US 869, 2 L Ed 2d 75), but exactness in the outcome of the audit method is not required (*Matter of Markowitz v. State Tax Commn.*, 54 AD2d 1023, 388 NYS2d 176, *affd* 44 NY2d 684, 405 NYS2d 454; *Matter of Cinelli*, Tax Appeals Tribunal, September 14, 1989). The taxpayer bears the burden of proving with

clear and convincing evidence that the assessment is erroneous (*Matter of Scarpulla v. State Tax Commn.*, 120 AD2d 842, 502 NYS2d 113) or that the audit methodology is unreasonable (*Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451; *Matter of Cousins Serv. Station*, Tax Appeals Tribunal, August 11, 1988). In addition, “[c]onsiderable latitude is given an auditor’s method of estimating sales under such circumstances as exist in [each] case” (*Matter of Grecian Sq. v. New York State Tax Commn.*, 119 AD2d 948, 501 NYS2d 219, 221).

D. In this case, the record establishes the Division’s clear and unequivocal written request for books and records of the corporation’s purchases, as well as the corporation’s failure to produce such books and records. The Division reasonably concluded that the corporation did not maintain or have available books and records that were sufficient to verify the amount of prepaid sales tax claimed for the audit period, including any cigarette purchase invoices. Having established the unavailability of required books and records, the Division was clearly entitled to attempt to verify the amount of prepaid sales tax claimed by contacting the corporation’s cigarette suppliers.

E. During the audit, the corporation failed to provide a complete set of cigarette purchase invoices or other source documentation to substantiate the amount of prepaid sales tax claimed on its sales tax returns for the period at issue. The auditor attempted to verify the amount claimed by contacting the corporation’s suppliers, but the documentation received from the suppliers in addition to that provided by the corporation established only a portion of such amount. Petitioners were assessed the amount of prepaid sales tax claimed but not substantiated.

As a general proposition, any imprecision in the results of an audit arising by reason of a taxpayer’s own failure to keep and maintain records of all of its purchases as required by Tax Law § 1135(e) must be borne by that taxpayer (*Matter of 88-02 Deli Grocery Corp.*, Tax Appeals Tribunal, September 13, 2012). Petitioners specifically complain that the amount of

prepaid sales tax claimed is correct, and that cigarette purchase invoices had been provided to the auditor. However, petitioners failed to adduce any source documentation, such as those purchase invoices, either on audit, at hearing or following the hearing, that would establish the actual amount of cigarette purchases throughout the audit period. Absent any records, petitioners' arguments do not provide any grounds for changing the Division's audit results. Therefore, it is concluded that petitioners have failed to carry their burden of showing the audit to be unreasonably inaccurate or clearly erroneous (*see Matter of Cook v. Tax Appeals Tribunal*, 222 AD2d 962 [1995]). Absent clear and convincing records of purchases, petitioners are not entitled to an additional adjustment (*Matter of 88-02 Deli Grocery Corp.*).

F. In establishing reasonable cause for the abatement of penalty, the taxpayer faces an onerous task (*Matter of Philip Morris, Inc.*, Tax Appeals Tribunal, April 29, 1993). In *Philip Morris* it was explained that “[b]y first requiring the imposition of penalties (rather than merely allowing them at the Commissioner’s discretion), the Legislature evidenced its intent that filing returns and paying the tax according to a particular timetable be treated as a largely unavoidable obligation [citations omitted]” (*Matter of MCI Telecommunications Corp.*, Tax Appeals Tribunal, January 16, 1992, *confirmed* 193 AD2d 978, 598 NYS2d 360 [1993]). Here, the corporation failed to make adequate books and records available for audit and substantially underreported and underpaid the tax due. Under these circumstances, the waiver of penalties is not justified.

G. The petitions of 4 U Convenience, Inc., and Ahmed Essani are denied, and the notices of determination, dated February 15, 2011 and February 16, 2011, respectively, as modified (*see* Finding of Fact 7), are sustained, together with such penalties and interest as may be lawfully due.

DATED: Albany, New York
April 10, 2014

/s/ Thomas C. Sacca
ADMINISTRATIVE LAW JUDGE